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No. 06-1005

IN THE

Supreme Court of the United States

UNITED STATES OF AMERICA,

Petitioner,

v.

EFRAIN SANTOS and BENEDICTO DIAZ,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF IN OPPOSITION OF RESPONDENT EFRAIN SANTOS

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TABLE OF CONTENTS

Page

TABLE OF CITED AUTHORITIES ii

STATEMENT 1

REASONS FOR DENYING THE PETITION 6

A. Whether or Not "Proceeds" Means Gross Receipts, There is No Financial Transaction in This Case Which Involves the Proceeds of a Specified Unlawful Activity. 6

B. The "Gross Receipts Versus Net Profits" Issue Should Be Addressed in the Context of Financial Transactions That Can Constitute Money Laundering, Rather Than Only the Predicate Unlawful Activity, So All Potential Meanings May Be Explored. 13

CONCLUSION 17

TABLE OF CITED AUTHORITIES

Page

Cases

Russello v. United States, 464 U.S. 16 (1983) 15

United States v. Awada, 425 F.3d 522 (8th Cir. 2005) 7, 12

United States v. Christo, 129 F.3d 578 (11th Cir. 1997) 7, 9

United States v. Conley, 37 F.3d 970 (3d Cir. 1994) 11

United States v. Dimeck, 24 F.3d 1239 (10th Cir. 1994) 8, 9

United States v. Edgmon, 952 F.2d 1206 (10th Cir. 1991) 10

United States v. Febus, 218 F.3d 784 (7th Cir. 2000) 4, 11, 14

United States v. Gaytan, 74 F.3d 545 (5th Cir. 1996) 8, 9

United States v. Grasso, 381 F.3d 160 (3d Cir. 2004) 16

United States v. Heap, 39 F.3d 479 (4th Cir. 1994) .. 10

Cited Authorities

Page

United States v. Iacaboni, 363 F.3d 1 (1st Cir. 2004) 12

United States v. Jackson, 935 F.2d 832 (7th Cir. 1991) 5

United States v. Johnson, 971 F.2d 562 (10th Cir. 1992) 7, 10

United States v. LeBlanc, 24 F.3d 340 (1st Cir. 1994) 10, 12

United States v. Lizza Indus., 775 F.2d 492 (2d Cir. 1985) 13

United States v. Mankarious, 151 F.3d 694 (7th Cir. 1998) 7, 9

United States v. McGahee, 257 F.3d 520 (6th Cir. 2001) 8

United States v. Milicia, 769 F. Supp. 877 (E.D. Pa. 1991) 13

United States v. Morelli, 169 F.3d 798 (3d Cir. 1999) 11

United States v. Pretty, 98 F.3d 1213 (10th Cir. 1996) 12

Cited Authorities

Page

United States v. Savage, 67 F.3d 1435 (9th Cir. 1995) 7

United States v. Scialabba, 282 F.3d 475 (7th Cir. 2002) 5, 15

United States v. Silvesti, 409 F.3d 1311 (11th Cir. 2005) 8

United States v. Valuck, 286 F.3d 221 (5th Cir. 2002) 15

Statutes

18 U.S.C. § 371 1

18 U.S.C. § 1955 ..... *passim*

18 U.S.C. § 1956 ..... *passim*

18 U.S.C. § 1957 7

18 U.S.C. § 1961 4

18 U.S.C. § 1963 13

28 U.S.C. § 2255 5

STATEMENT

Whether the term "proceeds" in 18 U.S.C. § 1956(a)(1) means "gross receipts" or "only the profits"—or something in between—is an issue this Court may need to address, but this is *not* a good case in which to do so. Even if, as the government contends, "proceeds" means gross receipts, this case does not present the predicate "financial transaction which in fact involves the proceeds of specified unlawful activity." 18 U.S.C. § 1956(a)(1). The only "financial transaction[s]" the government showed are collecting bets and paying winners. Those transactions are essential aspects of the "specified unlawful activity" itself—*i.e.*, "conduct[ing] . . . an illegal gambling business" under 18 U.S.C. § 1955. The question presented by the Petition should be addressed in a case that actually involves, as the government puts it, "conduct that *goes beyond the underlying crime* and entails use of the revenue produced by that crime." (Pet. 22 (emphasis added).)

1. Respondent Efrain Santos was charged with and convicted of running an illegal gambling business in violation of 18 U.S.C. § 1955 and of conspiring to run an illegal gambling business in violation of 18 U.S.C. § 371. Under § 1955, conducting a gambling business in violation of state or local law constitutes a federal crime. 18 U.S.C. § 1955(a). That statute, enacted as part of the Organized Crime Control Act of 1970, P.L. 91-452, 84 Stat. 922, states in pertinent part:

> § 1955. Prohibition of illegal gambling businesses

(a) Whoever conducts, finances, manages, supervises, directs, or owns all or part of an illegal gambling business shall be fined not more than $20,000 or imprisoned not more than five years, or both.

(b) As used in this section—

(1) "illegal gambling business" means a gambling business which—

(i) is a violation of the law of a State or political subdivision in which it is conducted;

(ii) involves five or more persons who conduct, finance, manage, supervise, direct, or own all or part of such business; and

(iii) has been or remains in substantially continuous operation for a period in excess of thirty days or has a gross revenue of $2,000 in any single day.

(2) "gambling" includes but is not limited to pool-selling, bookmaking, maintaining slot machines, roulette wheels or dice tables, and conducting lotteries, policy, bolita or numbers games, or selling chances therein.

The illegal gambling business Santos was convicted of running is known as a bolita, a type of lottery. The winning numbers in this bolita were based on the daily Pick Three and Pick Four Illinois lottery games and on the Puerto Rican Lottery. (Pet. App. 19a.) Santos had "runners" accept bets for his bolita primarily in bars and restaurants. (*Id.*) The runners would take a commission of 15-20% from the bet money and deliver the betting slips and the balance of the money to "collectors." (*Id.*) The collectors would then deliver the slips and bet money to Santos; before doing so, the collectors frequently took a "salary" out of the bet money and, on occasion, paid bolita winners who won $100 or less. (*Id.*) Santos paid the bolita's "big" winners. (*Id.*)

2. In addition, Santos was convicted of money laundering in violation of 18 U.S.C. § 1956(a) and of conspiring to commit money laundering in violation of 18 U.S.C. § 1956(h). Santos's money laundering convictions were for only "promotional" money laundering under § 1956(a)(1)(A)(i). That statute provides:

> (a)(1) Whoever, knowing that the property involved in a financial transaction represents the proceeds of some form of unlawful activity, conducts or attempts to conduct such a financial transaction which in fact involves the proceeds of specified unlawful activity—
>
> (A)(i) with the intent to promote the carrying on of specified unlawful activity;
>
> . . .
>
> shall be sentenced to a fine of not more than $500,000 or twice the value of the property

> involved in the transaction, whichever is greater, or imprisonment for not more than twenty years, or both. For purposes of this paragraph, a financial transaction shall be considered to be one involving the proceeds of specified unlawful activity if it is part of a set of parallel or dependent transactions, any one of which involves the proceeds of specified unlawful activity, and all of which are part of a single plan or arrangement.

18 U.S.C. § 1956(a)(1)(A)(i).

"Specified unlawful activity" is defined as "any act or activity constituting an offense listed in [18 U.S.C. § 1961(1)]." 18 U.S.C. § 1956(c)(7)(A). Among those offenses is conducting an illegal gambling business in violation of 18 U.S.C. § 1955.

3. Santos was sentenced to concurrent prison terms of 60 months for the illegal gambling convictions and 210 months for the money laundering convictions. (Pet. App. 18a, 20a.)

4. On direct appeal, Santos presented a single issue for review: whether "the evidence was insufficient to convict him of money laundering because his cash payments to the bolita's collectors and winners were essential transactions of the illegal gambling business, and thus cannot also constitute transactions under the promotion provision of the money laundering statute, 18 U.S.C. § 1956(a)(1)(A)(i)." *United States v. Febus*, 218 F.3d 784, 789 (7th Cir. 2000). The court of appeals upheld Santos's money laundering convictions, based on Seventh Circuit precedent that "[a] transaction satisfies the promotion provision of the

money laundering statute if it constitutes 'the practice of plowing back proceeds of [the illegal activity] to promote that activity.'" *Id.* at 789 (quoting *United States v. Jackson*, 935 F.2d 832, 842 (7th Cir. 1991)).

5. After *Febus*, the Seventh Circuit decided *United States v. Scialabba*, 282 F.3d 475 (7th Cir. 2002) (Easterbrook, J.), which addressed the meaning of the term "proceeds" in § 1956(a)(1) as it relates to business-like criminal activity. The court held that "at least when the crime entails voluntary, business-like operations, 'proceeds' must be net income; otherwise, the predicate crime merges into money laundering (for no business can be carried on without expenses) and the word 'proceeds' loses operational significance." *Id.* at 475.

6. Citing *Scialabba*, Santos pursued relief under 28 U.S.C. § 2255 arguing, among other things, the opinion in *Scialabba* required his convictions for money laundering be set aside and that he be re-sentenced. (Pet. App. 25a.) The district court, noting (as did the government) that the relevant facts of *Scialabba* are "amazingly similar" to those of Santos's case, found that Santos's money laundering convictions must be vacated under the holding of *Scialabba.* (Pet. App. 39a, 48a-49a)

7. The Seventh Circuit, on the government's appeal, upheld the district court's decision. (Pet. App. 1a-16a.)

REASONS FOR DENYING THE PETITION

A. Whether or Not "Proceeds" Means Gross Receipts, There is No Financial Transaction in This Case Which Involves the Proceeds of a Specified Unlawful Activity.

The question presented by the Petition—whether "proceeds" in § 1956(a)(1) means gross receipts or net profits from the specific unlawful activity—does not control the outcome of this case. That statute requires a "financial transaction which in fact involves" such proceeds. 18 U.S.C. § 1956(a)(1). There are no such transactions in this case which in fact involve the proceeds of a specified unlawful activity.

Rather, the only financial transactions the government showed here were transactions constituting the underlying specified unlawful activity—the operation of an illegal gambling business in violation of 18 U.S.C. § 1955(a). One type of financial transaction was the collection and delivery to Santos of the bet money and betting slips, with the "runners" and "collectors" deducting their compensation from the bet money before passing on the balance. (Pet. App. 19a.) If bets are not collected, no gambling business is conducted. If runners and collectors are not compensated, collection will not occur. Moreover, here the runners and collectors are also necessary to satisfy the statutory requirement that the business of illegal gambling "involve five or more persons who conduct, finance, manage, supervise, direct, or own all or part of such [illegal gambling] business." 18 U.S.C. § 1955 (b)(1)(ii). The other type of financial transaction was paying winnings to winning bettors. If winners are not paid, again no gambling business is conducted.

Section 1956(a)(1), in contrast, requires a transaction in the proceeds of specified unlawful activity *other than* the mere consummation of the unlawful activity itself. In the government's words, "conduct" is required "that goes beyond the underlying crime." (Pet. 22.) In the words of the government's cited authority (Pet. 20), what "matters" is "that the predicate offense has produced proceeds *in transactions distinct from* those transactions allegedly constituting money laundering." *United States v. Mankarious*, 151 F.3d 694, 706 (7th Cir. 1998) (emphasis added). In the more recent words of another circuit, "allegations of money laundering *that are inseparable from the underlying crime*, such as certain financial fraud transactions, have not withstood scrutiny." *United States v. Awada*, 425 F.3d 522, 524 (8th Cir. 2005) (emphasis added).

For example, the *Awada* court cited a case where money laundering convictions were reversed because "the withdrawal of [bank] funds charged as money laundering was one and the same as the underlying criminal activity of bank fraud and misapplication of bank funds." *United States v. Christo*, 129 F.3d 578, 581 (11th Cir. 1997). Put differently, there was no evidence that the defendant "engaged in a monetary transaction that was separate and in addition to the underlying criminal activity."[1] *Id*; *see also, e.g., United States v. Johnson*, 971 F.2d 562, 567-70 (10th Cir. 1992) (reversing money laundering convictions under § 1957 where

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[1] *Christo* involved money laundering charged under 18 U.S.C. § 1957. The Courts of Appeals agree that for purposes of the issue discussed above, "proceeds of specified unlawful activity" under § 1956(a)(1) and "criminally derived property" under § 1957 should be interpreted in the same manner. *E.g., Mankarious*, 151 F.3d at 704-05 & n.1; *United States v. Savage*, 67 F.3d 1435, 1442 (9th Cir. 1995).

the transactions alleged to constitute money laundering were the same wire transmissions necessary for the underlying wire fraud); *United States v. McGahee*, 257 F.3d 520, 528 (6th Cir. 2001) (reversing convictions because "[d]iverting the funds were part and parcel of the fraud and theft, and were not a separate act completed after the crime, as required under [§ 1956(a)(1)]").

Similarly, the court in *United States v. Dimeck*, 24 F.3d 1239 (10th Cir. 1994), reversed convictions under § 1956(a)(1) because the claimed money laundering transaction was the receipt and delivery of funds in payment for previously delivered illegal drugs. The court held that until payment for the drugs was made, "the underlying drug transaction had not yet been completed and the money laundering activity had not yet begun." *Id.* at 1246; *see also United States v. Gaytan*, 74 F.3d 545, 555-56 (5th Cir. 1996) ("funds do not become the proceeds of drug trafficking until a sale of drugs is completed. Hence, a transaction to pay for illegal drugs is not money laundering, because the funds involved are not the proceeds of an unlawful activity when the transaction occurs"; reversing convictions under § 1956(a)(1)).[2]

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[2] As indicated by some of the quotations above, courts often describe this issue in temporal terms, with a money laundering transaction required "after" the specified unlawful activity that generates the proceeds is "completed." Similarly, other cases provide that "because money laundering is an offense to be punished separately from an underlying criminal offense, the primary issue in a money laundering charge involves determining when the predicate crime becomes a completed offense after which money laundering can occur." *United States v. Silvesti*, 409 F.3d 1311, 1334 (11th Cir. 2005) (internal quotation marks omitted) (quoting *Christo*, 129 F.3d

(Cont'd)

Although the underlying crime may be structured to involve multiple transactions, either of necessity or as a matter of the criminal actor's choice, this does not alter § 1956(a)(1)'s requirement of a financial transaction in proceeds beyond the activities constituting the underlying crime. *See Gaytan*, 74 F.3d at 556 ("while it is true that several transactions took place, none involved the proceeds of unlawful activity"); *Dimeck*, 24 F.3d at 1246-47. With respect to selling illegal drugs, the court in *Dimeck* explained:

> A drug transaction, from a business perspective, consists of the distributor (or kingpin) getting the drugs to his middlemen who in turn either sell the drugs directly or have others conduct the actual street sales. The middlemen then collect the money from either their sellers or the consumer (depending upon whether they conduct the sales themselves) and the middlemen then pay the distributor for the drugs that had been advanced to them. It is not unusual for a middleman to use a courier to deliver the money to, and pick up the drugs from, the distributor.

(Cont'd)

at 579-80). While classic money laundering involves first the completion of the underlying crime and then subsequent laundering of the proceeds, other cases have held that money laundering can occur in some situations lacking this temporal sequence. *E.g., Mankarious*, 151 F.3d at 703-06. As discussed in the text and as *Christo* alternatively states, the substantive point is not temporal sequence (although it is convenient and usually accurate to speak in such terms), but rather that money laundering requires a financial transaction "in addition to the underlying criminal activity." 129 F.3d at 581.

24 F.3d at 1246-47 (footnote omitted). Similarly here, the predicate crime of conducting an illegal gambling business may involve several transactions—and always must involve collecting bet money and paying winners.

The widely acknowledged purpose of § 1956(a)(1) itself shows that the transaction or transactions constituting the underlying crime cannot be the "financial transaction which in fact involves the proceeds of [that crime]." *Id.* Congress "intended money laundering to be a separate crime distinct from the underlying offense that generated the money." *United States v. LeBlanc*, 24 F.3d 340, 346 (1st Cir. 1994) (citing *Johnson*, 971 F.2d at 569, and *United States v. Edgmon*, 952 F.2d 1206, 1213 (10th Cir. 1991)). The purpose was *not* to provide "an alternative means of punishing the prior 'specified unlawful activity.'" *United States v. Heap*, 39 F.3d 479, 486 (4th Cir. 1994) (quoting *Edgmon*, 952 F.2d at 1214). Rather, "'Congress intended . . . to punish activity that was not previously punished criminally,'" *Dimeck*, 24 F.3d at 1244 (quoting *Edgmon*, 952 F.2d at 1214), and thereby to fill "'the gap in the criminal law with respect to the post-crime hiding of the illgotten gains.'" *Johnson*, 971 F.2d at 569 (quoting *Edgmon*, 952 F.2d at 1213).

The only transactions involved here—runners and collectors withholding from bet money compensation for their bet-collecting and delivery, and Santos and collectors paying winners—are not "separate crime[s] distinct from the underlying offense that generated the money," *i.e.*, conducting an illegal gambling business. Rather, that activity *was* "previously punished criminally" by § 1955. Section 1956(a)(1) was not intended to provide "an alternative means of punishing" that same activity.

Perhaps adverting to this issue indirectly, the government says that "'proceeds are derived from an already completed offense, *or a completed phase of an ongoing offense*.'" (Pet. 21 (emphasis added) (quoting *United States v. Conley*, 37 F.3d 970, 980 (3d Cir. 1994).) However, the key words in the italicized phrase are "ongoing offense." The transactions constituting money laundering in *Conley* followed *completed* crimes, even though the overall scheme (there, conducting an illegal gambling business) continued. The court reiterated *Edgmon*'s point that money laundering under § 1956 is "intended . . . to apply to transactions occurring after the completion of the underlying criminal activity," and noted that the money laundering transactions there involved the disposition of monies "collected from the [video] poker machines" in "various business establishments" where the "gambling activity occurred." 37 F.3d at 980. In other words, the "proceeds" of conducting an illegal gambling business in *Conley* was money that remained after the bets were collected and the winners were paid. *Id.*; *see also United States v. Morelli*, 169 F.3d 798, 804 (3d Cir. 1999) (explaining that "[t]he money laundering aspect of the scheme [in *Conley*] derived from the retrieval and distribution of the money deposited in the machines" after "the specified unlawful activity had been completed").[3]

The government also points out the *Febus* court's reasoning that an "illegal gambling operation . . . could not

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[3] *Conley* involved a double jeopardy challenge to the money laundering statute rather than an argument directly addressing the statutory meaning of proceeds (or financial transaction involving proceeds). Whether or not *Conley* is correct on its facts concerning the statutory meaning (*see* Part B, *infra*), those facts involved more than the core gambling business activity of collecting bet money and paying winners, which is all the government showed in this case.

grow and prosper if it did not compensate its employees and pay winners." (Pet. 21.) *See also United States v. Iacaboni*, 363 F.3d 1, 5 (1st Cir. 2004). Whether or not correctly decided, those cases addressed only whether these types of transactions satisfy the "promotion" requirement of § 1956(a)(1)(A)(i). The issue here, by contrast, is whether they are even the predicate "financial transaction[s] which in fact involve[] the proceeds of specified unlawful activity" under subsection (a)(1). A business operation which fails to collect bet money—whether because it does not "compensate its employees" to do the collection or otherwise—and which does not "pay winners," is not an illegal gambling business; it therefore is not a "specified unlawful activity."

The government might also point out that there are situations in which the money laundering transaction may occur simultaneously with consummation of the underlying crime. *See LeBlanc*, 24 F.3d at 347 (when bet money was collected after bets were lost, defendant had losing gamblers pay by checks to fictitious payees to conceal the source of the funds); *United States v. Pretty*, 98 F.3d 1213, 1221 (10th Cir. 1996) (defendant had illegal kickbacks "filtered through real estate transactions" to conceal source of money). Whether these situations are considered to involve simultaneous transactions (one the underlying criminal activity, the other money laundering) or different components of a single transaction, they involve conduct that goes beyond the mere consummation of the specified unlawful activity. No such facts are presented in this case. Again, the only financial transactions the government showed—involving the collection of bet money and paying winners—are "inseparable from the underlying crime." *Awada*, 425 F.3d at 524.

B. The "Gross Receipts Versus Net Profits" Issue Should Be Addressed in the Context of Financial Transactions That Can Constitute Money Laundering, Rather Than Only the Predicate Unlawful Activity, So All Potential Meanings May Be Explored.

The potential meanings of proceeds are not necessarily limited to "gross revenues" on the one hand and "net profits" on the other. Most obviously, "proceeds" may mean gross profits—*i.e.*, gross receipts less only direct costs—as some courts have held under the RICO forfeiture statute, 18 U.S.C. § 1963(a)(3). *See United States v. Lizza Indus.*, 775 F.2d 492, 498 (2d Cir. 1985); *United States v. Milicia*, 769 F. Supp. 877, 887-89 (E.D. Pa. 1991). This interpretation is also supported by the legislative history the government quotes, which does not adopt a "gross receipts" definition of "proceeds" but rather says that "*overhead* expenses" need not be deducted. (Pet. 13 (emphasis added) (quoting S. Rep. No. 225, 98th Cong., 1st Sess. 199 (1983)).)

Defining "proceeds" as gross profits would resolve the government's expressed concerns about a perceived "unreasonable burden of proof" and the need for "generally accepted accounting principles for criminal enterprises." (Pet. 11, 15.) The weight properly given to these contentions, however, should be evaluated in light of the many computational methods the government has been permitted to use in the absence of accounting records. *See, e.g.*, *Milicia*, 769 F. Supp. at 885-86 (discussing cases). In any event, this case does not provide a factual context in which to assess the government's concerns. Here, the government apparently made no effort to determine gross or net profits, or to show that any bet monies (not even gross revenues) were actually

"reinvested" in the ongoing illegal gambling business.[4] This despite the facts that Santos had both "records" and an accountant, from which the government showed "the income to [Santos's] bolita expanded from approximately $250,000.00 per year for the years 1989 to 1992, to $330,000.00 for 1993, and up to $410,000.00 for 1994." *Febus*, 218 F.3d at 790.[5]

The government also admittedly made no attempt to show net profits or gross profits over any period of time. (Gov't Appellant's Br. at 7.) Indeed, it may have been the government's strategy not to make such a showing, but rather to pursue a theory that the transactions constituting the underlying crime also constitute a) transactions in proceeds satisfying § 1956(a)(1), and b) promotion satisfying

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[4] The use of the term "reinvesting" in *Febus* does not provide this factual context here, as that term was used in relationship with the promotional challenge at issues in that case and was used to prove the time period requirement of § 1955 (b)(1)(iii). *Febus*, 218 F.3d at 790. The *Febus* court did speak of "plowing back proceeds" and "reinvest[ing] the bolita's proceeds. (Pet. 4, 5 (quoting 218 F.3d 789, 90).) All the court meant by these terms, however, was again runners and collectors deducting compensation from bet money and Santos and collectors paying winners. There is no showing of any other financial transaction in this case as the government has admitted. (Gov't Appellant's Br. 7.) In particular, there is no evidence of transactions that in any normal sense would be called "plowing back" or "reinvest[ment]."

[5] This increase in gross receipts was Seventh Circuit's basis for finding that compensating bet collectors and paying winners "promoted" the illegal gambling business within the meaning of § 1956(a)(1)(A)(i). *Febus*, 218 F.3d at 790. Santos disagreed with that reasoning, of course, but that is not the issue here.

§ 1956(a)(1)(A)(i). But whatever the reason, the government did not build a record for evaluating accounting issues.

Depending upon contexts that do not exist here, further refinement of the meaning of "proceeds" is possible. For example, the post-crime transactions claimed to constitute money laundering in *Scialabba* included dividing the contents of video poker machines with the owner of the business establishment to cover winnings the owner had paid to bettors. 282 F.3d at 476. Fact patterns like that pose the issue whether financial transactions in proceeds include payments for direct expenses previously incurred as part of the underlying criminal activity.[6]

This Court has previously been sensitive to the existence of issues like these and the need to address them in cases in which they are actually presented. *See Russello v. United States*, 464 U.S. 16, 29 n.3 (1983) ("In our ruling today, we recognize that we have not resolved any ambiguity that might be inherent in the terms 'profits' and 'proceeds.' Our use of those terms is not intended to suggest a particular means of calculating the precise amount that is subject to RICO forfeiture in any given case."). The instant case, in which the only financial transactions shown were those constituting the underlying criminal activity itself, is not a suitable vehicle for exploring these issues. The government asks the Court to consider the "proceeds" issue as if it involved a choice

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[6] The above issue shades into the question whether transactions with proceeds can meaningfully be said to promote *prior* specified unlawful activity under § 1956(a)(1)(A)(i)—an issue on which the circuits are split. *Compare United States v. Valuck*, 286 F.3d 221, 227 n.5 (5th Cir. 2002) (discussing cases on both sides of circuit split) *with* Pet. App. 10a-12a (discussing cases contrary to *Scialabba*).

between only two possible positions and an answer that must apply uniformly regardless of context—*i.e.*, "proceeds" is either gross receipts or net profits, period. (*See* Pet. I.) As shown, however, other alternatives exist which cannot be explored on these facts.

Moreover, the general issue of whether "proceeds" in § 1956(a)(1) means "gross receipts . . . or only the profits," (Pet. I), is both more difficult and more complex than the government's Question Presented makes it appear. In addition to the alternative meanings of "proceeds" discussed above, the court in *Scialabba* concluded, on nearly identical facts as presented here, that proceeds means profits, at least when a case involves "voluntary, business-like operations." 282 F.3d at 475. At a minimum, this includes conducting an illegal gambling *business*. But regardless of the extent of *Scialabba*'s holding, when a business-like activity is being conducted (as here), a profits definition of proceeds both is correct and avoids the concerns cited by the court in *Scialabba*. Thus, and if not universally so at least in the context of running an illegal gambling business, a profits definition is both "well-argued and intuitively appealing." *United States v. Grasso*, 381 F.3d 160, 167 (3d Cir. 2004).

For all the foregoing reasons, this is not a good case for the Supreme Court to address the meaning of "proceeds" as a stand-alone issue.

CONCLUSION

The petition for a writ of certiorari should be denied.

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